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October 30, 2012

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## VIA HAND DELIVERY

Ms. Bridget Bohac  
Chief Clerk  
Texas Commission on Environmental Quality  
12100 Park 35 Circle  
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Austin, TX 78753

Re: TCEQ Docket No. 2012-1662-MIS-U  
Appeal of Negative Use Determination  
Tax Relief for Pollution Control Property Program  
Application No. 12203; Ennis Power Plant, Ellis County

Dear Ms. Bohac:

Please find enclosed *Ennis Power Company, LLC's Reply to the Response Briefs filed by the Executive Director and Public Interest Counsel* in the above-referenced matter.

Ennis Power Company, LLC hopes that an agreed resolution of the dispute regarding the appropriate tax relief for heat recovery steam generators ("HRSGs") can be achieved, and requests a meeting with the Executive Director's staff to discuss the treatment of HRSGs under Chapter 17.

If you have any questions concerning this filing, please do not hesitate to contact me at the number above.

Sincerely,



Whitney L. Swift

Enclosures

cc: Service List

**TCEQ Docket No. 2012-1662-MIS-U**

|                                     |          |                                    |
|-------------------------------------|----------|------------------------------------|
| <b>APPEAL OF THE EXECUTIVE</b>      | <b>§</b> | <b>BEFORE THE TEXAS COMMISSION</b> |
| <b>DIRECTOR'S USE DETERMINATION</b> | <b>§</b> |                                    |
| <b>ISSUED TO ENNIS-TRACTEBEL</b>    | <b>§</b> | <b>ON</b>                          |
| <b>POWER COMPANY, LP</b>            | <b>§</b> |                                    |
|                                     | <b>§</b> |                                    |
| <b>APPLICATION NUMBER 12203</b>     | <b>§</b> | <b>ENVIRONMENTAL QUALITY</b>       |

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**APPEAL OF THE EXECUTIVE DIRECTOR'S NEGATIVE USE DETERMINATION  
ENNIS POWER COMPANY, LLC'S REPLY TO THE RESPONSE BRIEFS  
FILED BY THE EXECUTIVE DIRECTOR AND PUBLIC INTEREST COUNSEL**

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TO THE HONORABLE COMMISSIONERS AND GENERAL COUNSEL OF THE TEXAS  
COMMISSION ON ENVIRONMENTAL QUALITY:

Ennis Power Company, LLC ("Ennis Power") submits this Reply to the Response Briefs filed by the Texas Commission on Environmental Quality's ("TCEQ's") Executive Director ("ED") and Office of Public Interest Counsel ("OPIC") in Ennis Power's appeal of the ED's negative use determination issued under the TCEQ's Tax Relief for Pollution Control Property Program, also known as the "Proposition 2" program. For the reasons set forth below and in Ennis Power's Appeal of the Executive Director's Negative Use Determination filed August 2, 2012, Ennis Power respectfully requests that the Commission overturn the ED's negative use determination for the heat recovery steam generator ("HRSG") installed at the Ennis Power Plant and remand the matter to the ED for a new, positive use determination that recognizes the significant air quality benefits and pollution reductions achieved by Ennis Power's HRSG.

**BACKGROUND**

Ennis Power filed an "Application for Use Determination for Pollution Control Property" on April 21, 2008, seeking a partial positive use determination for a HRSG that had been installed at the Ennis Power Plant located in Ellis County ("the Application"). A copy of the Application is included as **Exhibit A**. The Application sought a Tier IV partial use determination for the HRSG, which had been installed at the plant in 2002.

On April 24, 2008, the ED sent a letter to Ennis Power's designated contact stating that the Application had been declared administratively complete.<sup>1</sup> A copy of that administrative completeness determination letter is included as **Exhibit B**. The ED assigned the Application number 07-12203. The ED notified the Ellis County Appraisal District of the Application on April 22, 2008. On May 1, 2008, the ED issued a number of 100% positive use determinations for HRSGs under the Proposition 2 program.

County appraisal districts filed notices of appeal for six of the 25 Proposition 2 HRSG applications for which the ED had granted a full 100% positive use determination. The ED's response brief in the 2008 appraisal district appeal, which is included as **Exhibit C**, describes the ED's efforts to develop a uniform use determination percentage for HRSGs. The ED assembled a Workgroup comprised of HRSG applicants, appraisal district representatives and other interested parties. *See Exhibit C*, ED's 2008 Response Brief, at 10-11. Based on the Workgroup's efforts, the ED recommended a 61% positive use determination for HRSGs in a combined cycle facility like that at the Ennis Power plant. *Id.* at 11.

The ED's 2008 response brief gives no indication that the ED or its Workgroup challenged whether HRSGs are used for pollution control purposes. In fact, the Workgroup reached the following conclusions with regard to HRSGs:

A comparable combined cycle power plant produces less air emissions than the same size simple cycle power plant. The reduced emissions are attributed to reduced combustion. The installation of the HRSGs lead to the reduced emissions.

The pollution control aspect of the combined cycle power plant relates solely to the installation of the HRSGs. However, installation of HRSG also results in increased efficiency and production gain.

*Id.* at 10. Similarly, the ED's recommended partial positive use determination must be based on a determination that HRSGs meet Proposition 2 standards for providing an environmental benefit. The Commission did not act on the 2008 appeal, however, and the 6 HRSG applications that were the subject of the appeal remained pending until July 2012. For 19 of the ED's initial

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<sup>1</sup> Based on the date of application submittal and the administrative completeness determination, Ennis Power's application should be governed by the version of Chapter 17 that became effective on February 7, 2008, which included Tier IV applications. Neither the ED nor OPIC dispute this issue regarding rule applicability. *See* ED Response Brief at 3; OPIC Response Brief at 4.

25 HRSG 100% positive use determinations, however, the ED's determination was final and remains in effect. Copies of those 19 final positive use determination letters for HRSGs are included as **Exhibit D**.

Ennis Power's application was not part of the initial group of applications for which the ED issued a positive use determination, nor was it part of the 2008 appeal process. The ED did not act on Ennis Power's application until July 10, 2012.<sup>2</sup> Over four years after Ennis Power filed its Proposition 2 application, the ED issued a "Notice of Negative Use Determination" for the HRSG in the Application, included as **Exhibit E**. The Notice of Negative Use Determination asserted, as the basis for the determination, that "[h]eat recovery steam generators are used solely for production; therefore, are not eligible for a positive use determination." The Notice included no technical support document or other information or materials in support of the ED's determination.

On August 2, 2012, Ennis Power timely filed an appeal of the ED's negative use determination in accordance with 30 TEX. ADMIN. CODE ("TAC") § 17.25(b). The TCEQ's General Counsel subsequently established a briefing schedule for the Proposition 2 HRSG appeals, and the ED and OPIC filed briefs in response to Ennis Power's appeal on October 4, 2012. Given the overlapping nature of the HRSG tax appeals, the ED filed a single, consolidated brief for all of the pending HRSG appeals. Ennis Power files this Reply Brief in accordance with the General Counsel's briefing schedule and as a supplement to its Application and August 2, 2012 appeal filing.

### ARGUMENT

The ED's negative use determination for Ennis Power's HRSG application represents a complete and unexpected reversal of ED policy. The determination ignores the significant environmental benefits provided by HRSGs that the ED had previously recognized.

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<sup>2</sup> Under 30 TAC § 17.12, *Application Review Schedule*, the ED was required to complete the technical review of the Application (submitted as a Tier IV application) within 30 days of receipt of the required application materials. See 30 TAC § 17.12(3) (effective February 7, 2008); see also 30 TAC § 17.12(3) (current). Even if the Commission issues a positive use determination for the Ennis Power Plant HRSG/combustion turbine installation in response to this appeal, the delay in the ED's ruling on the Application will have prejudiced Ennis Power by depriving Ennis Power of the full tax reduction benefit flowing from the determination from 2009 to present -- particularly when compared to other applicants who filed applications for use determinations for similar HRSG installations in early 2008 and were granted full positive use determinations by the ED in May 2008. The Ellis County Appraisal District has granted Ennis Power partial tax relief for the HRSGs in the Application prior to the ED's determination, but Ennis Power has not received the full tax relief granted to those HRSG owners with full positive use determinations.

Rather than make a determination that recognizes both the pollution control benefit and the production value of HRSGs, the ED has defaulted to a position that is contrary to the plain language of the Texas Tax Code and made a decision that runs contrary to Texas constitutional principles of fair and uniform taxation. The Commission should overturn the ED's negative use determination and remand the Application to the ED for a determination that recognizes the pollution reduction benefits of Ennis Power's HRSG.

## **I. HRSGs Reduce Air Pollution in Texas**

The ED's change in position and this appeal present a key issue for the Commission's determination: is tax relief under the Proposition 2 program limited to add-on emissions control equipment, or will the TCEQ grant relief under the program for devices like HRSGs that do not "control" emissions, but clearly "prevent" emissions by generating additional power *without* increasing emissions?

The ED asserts, contrary to statute,<sup>3</sup> and to his own prior statements on the subject, and to and common sense, that "HRSGs do not provide an environmental benefit." OPIC defers to the ED in its response brief, but notes that the negative use determination letter provides no information as to why the ED no longer considers HRSGs to be qualifying pollution control equipment.

HRSGs use waste heat to reduce emissions of oxides of nitrogen ("NOx"), sulfur dioxide ("SO<sub>2</sub>") and other pollutants from power generation activities on a pound-per-kilowatt hour basis. As the ED stated in his 2008 HRSG appeal response brief,

A HRSG acts as a fuel substitute in a typical combined-cycle installation. . . . This process eliminates the need for the additional burning of coal or other hydrocarbon based fuel in order to obtain the same increase in electrical energy generation output at the site.

**Exhibit D**, ED's 2008 Response Brief, at 6. It cannot be reasonably disputed that the use of a HRSG in power generation is an emissions-reducing process for generating power. The ED, however, now asserts that this is not an "environmental benefit." In doing so, the ED appears to make a distinction not found in the Texas Tax Code or Chapter 17 between "add-on" emissions

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<sup>3</sup> As discussed in greater detail in section III below, the Texas Tax Code includes HRSGs on its "list of facilities, devices, or methods for the control of air, water, or land pollution." TEXAS TAX CODE § 11.31(k).

control devices and a device like a HRSG that, through efficiency gains, will allow for more power generation with the same amount of air pollution.<sup>4</sup>

The Proposition 2 program is designed to provide tax relief for “personal property that the person owns and that is used wholly or partly as a facility, device, or method for the control of air, water, or land pollution.” TEXAS TAX CODE § 11.31(a). Nothing in the Texas Tax Code or the Commission’s Chapter 17 rules preclude devices like HRSGs from qualifying for tax relief -- as evidenced by the ED’s decision to grant a number of full (100%) positive use determinations for HRSGs *after* the date that Ennis Power filed its application. The Executive Director was correct in 2008 to acknowledge that HRSGs provide an environmental benefit by reducing the amount of air pollution resulting from power generation as a “fuel substitute.” The ED continued to recognize the environmental benefit of HRSGs in the stakeholder process that followed, as the ED worked with interested appraisal districts and HRSG owner/operators to identify a partial positive use determination amount for HRSGs -- work that *presumed* an environmental benefit from HRSGs.

The ED’s 2012 reversal shocked Ennis Power and other HRSG owners who had submitted Proposition 2 applications to the TCEQ. Equally surprising is the ED’s new assertion that HRSGs do not provide an environmental benefit. HRSGs *do* provide an environmental benefit, by reducing fuel consumption and by reducing the amount of NO<sub>x</sub>, SO<sub>2</sub> and other pollutants emitted by the generation that powers Texas.

## **II. The Role that a HRSG Plays in Production Does Not Preclude a Positive Use Determination**

The ED states in his July 10, 2012 Negative Use Determination Letter to Ennis Power that HRSGs are not eligible for a positive use determination under the Proposition 2 program because they “are used solely for production.” The ED maintains that position in his

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<sup>4</sup> The United States Environmental Protection Agency (“EPA”) has long recognized energy efficiency as a form of pollution prevention. See EPA Memorandum from F. Henry Habicht II, Deputy Administrator, *EPA Definition of “Pollution Prevention”* at p. 3 (May 28, 1992) <<http://epa.gov/region07/air/nsr/nsrmemos/pollprev.pdf>>. More recently, EPA recognized the pollution control benefits of HRSG operation in commenting on a state permitting authority’s best available control technology (“BACT”) analysis. In a 2012 letter to the Wisconsin Department of Natural Resources, EPA ordered state officials to consider combined cycle turbines (which incorporate a HRSG) as part of the BACT review for a proposed simple cycle gas-fired electric generating unit (which did not incorporate a HRSG). See EPA Region 5, Letter to Wisconsin Department of Natural Resources (March 15, 2012) <<http://epa.gov/nsr/ghgdocs/20120315Milwaukee.pdf>>. EPA stated that the combined cycle unit should be considered because “[c]ombined cycle turbines are generally more energy efficient than simple cycle turbines.”

Response Brief. OPIC defers to the ED in its response brief. Ennis Power acknowledges that HRSGs generate power. That production benefit, however, does not preclude HRSGs from qualifying for tax relief under the Proposition 2 program.

A HRSG generates additional power *without increasing air pollution* from the gas-fired turbine to which it is attached. The ED's 2012 position on HRSGs takes an all-or-nothing approach that ignores both the emissions reduction benefit of a HRSG *and* the clear direction in the Texas Tax Code that the TCEQ should, for equipment that has a production benefit, distinguish the proportion of the property that is used for production from the "proportion of property that is used to control, monitor, prevent, or reduce pollution." TEXAS TAX CODE § 11.31(a).

The ED cites Attorney General Opinion JC-0372 in his response brief. In JC-0372, the Attorney General confirmed that both add-on pollution control devices *and* methods of production that limit pollution are entitled to a tax exemption under the Proposition 2 program. Texas Attorney General Opinion No. JC-0372 (2001). In that opinion, the Attorney General states,

Next, we consider whether section 11.31 excludes from its scope pollution-reducing production equipment. Significantly, the statute applies to property used "wholly or partly" for pollution control. . . . The term "partly," however, embraces property that has only *some* pollution-control use. This broad formulation clearly embraces more than just add-on devices. Furthermore, that statute clearly embraces not only "facilities" and "devices" but also "methods" that prevent, monitor, control, or reduce pollution. "Methods" is an extremely broad term that clearly embraces means of production designed, at least in part, to reduce pollution.

Based on its plain language and the common meaning of the terms "wholly," "partly," and "method," we conclude that section 11.31 clearly extends to, in your words, "equipment . . . that is used to make a product and by its design limits pollution."

*Id.* at 5 (references omitted) (emphasis added). The ED misreads JC-0372 in arguing that it simply reiterates the ED's role in distinguishing the proportion of property that is used to reduce pollution from the proportion of property that is used to produce goods or services. While the ED has that role in the Proposition 2 program, *see* TEXAS TAX CODE § 11.31(g)(3), the ED's

Response Brief mischaracterizes JC-0372 and fails to recognize the Attorney General's endorsement of Proposition 2 tax exemptions for "pollution-reducing production equipment."

Ennis Power's HRSG is pollution-reducing production equipment. The HRSG generates power, but does so without burning additional fuel and without adding to the emissions generated by the gas turbine, allowing for greater energy production for the same amount of combustion emissions. Use of the HRSG decreases air pollution on a pound-of- emissions-per-kilowatt basis, and the fact that the HRSG has a production component does not preclude that property from qualifying for tax relief under the Proposition 2 program.

### **III. The Executive Director has Incorrectly Dismissed the Importance of HRSGs Being Listed in Texas Tax Code § 11.31(k)**

The ED and OPIC argue that the inclusion of HRSGs in the Texas legislature's list of methods for the control of air, water, or land pollution does not entitle HRSGs to a positive use determination. The legislature's decision to include HRSGs on the list does not guarantee a 100% positive use determination, but it does reflect the legislature's determination that HRSGs are either "wholly or partly" used for control of air pollution.

Texas Tax Code § 11.31(k) directs the TCEQ to develop rules establishing a list "of facilities, devices, or methods for the control of air, water, or land pollution" and states that the list must include HRSGs. *See* TEXAS TAX CODE § 11.31(k) & (k)(8). The list of devices in § 11.31(k), which was then codified at Figure: 30 TAC § 17.14(a), Part B, is known as the Expedited Review List.<sup>5</sup> Tax Code § 11.31(m), which the ED quotes in his Response Brief, establishes the ED's obligations when a Proposition 2 application is filed for HRSGs or any other of the Expedited Review List items from the statute. The ED "shall determine that the facility, device, or method described in the application is used *wholly or partly* as a facility, device, or method for the control of air, water or land pollution." *Id.* § 11.31(m). The ED is *not* directed to determine "whether or not" the devices listed in § 11.31(k) are used as for pollution control purposes; rather, the inquiry is *how much* of the device should be considered to be for pollution control. *See id*; *see also* 30 TAC § 17.17(d) (2008 version) ("For applications containing only property falling under a category listed in Part B of the Equipment and

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<sup>5</sup> The Expedited Review List is currently codified at 30 TAC § 17.17(b), Figure: 30 TAC § 17.17(b).



Categories List, located in § 17.14(a) of this title (relating to Equipment and Categories List), *a use determination must be calculated.*”) (emphasis added).

The legislature selects the words, phrases, and expressions in statutes deliberately and purposefully. *See Texas Lottery Comm’n v. First State Bank of DeQueen*, 235 S.W.3d 628, 635 (Tex. 2010); *Shook v. Walden*, 304 S.W.3d 910, 917 (Tex. App.--Austin 2010, no pet.). Under the Code Construction Act, “the entire statute is intended to be effective.” TEX. GOV’T CODE § 311.021(2). By issuing a negative use determination for Ennis Power’s HRSG, the ED has acted in a way that is inconsistent with how the legislature classified HRSGs for purposes of the Proposition 2 program, and is inconsistent with how the legislature intended the Texas Tax Code to operate.

The ED, in implementing the Proposition 2 program on behalf of the TCEQ, does not have any power inconsistent with the powers that the legislature delegated to the TCEQ. *Public Utility Comm’n v. City Pub. Serv. Bd.*, 53 S.W.3d 310, 312 (Tex. 2001). The TCEQ’s primary objective must be to give effect to the legislature’s intent, via the statutory text. *State v. Shumake*, 199 S.W.3d 279, 284 (Tex. 2006); *Lexington Ins. Co. v. Strayhorn*, 209 S.W.3d 83, 85 (Tex. 2006). The legislature included HRSGs on the § 11.31(k) list of devices for the control of pollution, and directed the ED to determine if such devices are “wholly or partly” used for pollution control. *See* TEXAS TAX CODE § 11.31(k) & (m). The ED has acted outside the clear direction of the legislature in its treatment of HRSGs. As such, its treatment of HRSGs is arbitrary and capricious. *See Rodriguez v. Service Lloyds Ins. Co.*, 997 S.W.2d 248, 254-55 (Tex. 1999).<sup>6</sup>

The ED cites statements in the regulatory history of the Proposition 2 program in support of its discretion to issue a negative use determination for Expedited Review List devices that are governed by sections 11.31(k) and (m) of the Texas Tax Code. Those statements, and

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<sup>6</sup> The ED’s decision also runs afoul of Texas Tax Code § 11.31(l) requirements regarding the removal of an item from the Expedited Review List. Under § 11.31(l), the TCEQ is directed to update the Expedited Review List at least once every three years, and can remove an item from the Expedited Review List. *See* TEX. TAX. CODE § 11.13(l); *see also* 30 TAC § 17.17(b). However, deleting an item from the Expedited Review List must be accompanied by a Commission finding of “compelling evidence to support the conclusion that the item does not provide pollution control benefits.” *Id.* No such finding has been made with regard to HRSGs, and the TCEQ has not removed HRSGs from the Expedited Review List or initiated procedures to remove HRSGs from the Expedited Review List. If HRSGs provide no pollution control benefit, as now alleged by the ED, they should have been removed from the Expedited Review List. That has not happened, because HRSGs *do* provide a pollution control benefit.

the ED's conclusion in this matter that HRSGs are neither wholly *nor* partly used for air pollution control, contradict the plain language of the Texas Tax Code. The TCEQ must give effect to the unambiguous language of the Texas Tax Code and remand this matter to the ED for a new determination consistent with the governing legislation.

#### **IV. Ennis Power Cited Valid and Applicable Regulations in its Application**

The ED argues in its Response Brief that Ennis Power and the other HRSG applicants failed to cite a qualifying environmental regulation in their Proposition 2 applications. In fact, the ED -- for the first time, over four years since Ennis Power filed its Proposition 2 applications -- issues a wholesale rejection of every rule cited in every HRSG application, arguing that none of the cited regulations require the installation of a HRSG.

Ennis Power cited the following TCEQ rule in its Proposition 2 application: 30 TAC § 117.1310. Section 117.1310 satisfies Ennis Power's obligation to identify a qualifying rule under the Proposition 2 program. Under 30 TAC § 17.4, the pollution control property "must be used, constructed, acquired, or installed wholly or partly to meet or exceed laws, rules, or regulations adopted by any environmental protection agency . . . for the prevention, monitoring, control, or reduction" of pollution. 30 TAC § 17.4(a). The rule cited in Ennis Power's application establishes NOx emission limits for stationary gas turbines in the Dallas-Fort Worth ozone nonattainment area.

In support of its wholesale rejection of Ennis Power's (and every other HRSG applicants') cited regulations, the ED argues that there is "an insufficient nexus" between the HRSG and the cited rules, because those rules do not require the installation of the HRSG. The ED's new "nexus" requirement is not part of the statutory Proposition 2 program or the TCEQ's implementing regulations, and inserting this requirement is unfair and arbitrary when compared to other Proposition 2 HRSG applications.

Ennis Power's gas turbine and HRSG is subject to the Chapter 117 NOx and carbon monoxide ("CO") limits. Ennis Power uses the HRSG increase to the power generating output of the gas turbine while still complying with these emission limits. Importantly, nothing in the Texas Tax Code or Chapter 17, or in any Attorney General Opinion or case addressing the Proposition 2 program, includes the ED's new requirement that the application specify a rule

“that requires the installation” of the specific pollution control equipment. This “nexus” requirement is simply not found anywhere but in the ED’s Response Brief.

The ED’s move to raise an alleged deficiency in Ennis Power’s application at this stage of the process also runs afoul of Chapter 17. Under Chapter 17 in effect at the time that Ennis Power submitted the Application, if an application was deficient, the ED was to inform the application that the application is *not* administratively complete and that it is deficient within three days of receipt of the application. *See* 30 TAC § 17.12(2).<sup>7</sup> The applicant is then provided an opportunity to correct the deficiency. *Id.* § 17.12(2)(A). In this case, however, the ED informed Ennis Power that its application *was* administratively complete, as shown by **Exhibit B**. Ennis Power had no indication that its application was deficient based on the rules cited in the application, or for any other reason, until receipt of the negative use determination in July 2012. The ED’s rejection of Ennis Power’s application based on the alleged failure to provide a qualifying regulation is invalid and further grounds for the Commission’s remand of the decision.

#### **V. The Texas Constitution Prohibits the Executive Director’s Reversal on HRSGs under the Proposition 2 Program**

The ED claims that its reversal in the treatment of HRSGs under the Proposition 2 program does not violate the uniform taxation requirements of the Texas Constitution or the Texas Tax Code. The cases cited by the ED do not establish or support the ED’s change in interpretation here, because the ED’s new position is inconsistent with the requirements of the Texas Tax Code.

Article VIII, Section I of the Texas Constitution states that “[t]axation shall be equal and uniform.” TEX. CONST. art. VIII, § 1(a). The legislature incorporated that same constitutional principle into the laws establishing the Proposition 2 program, directing the TCEQ to adopt rules to implement the program and stating that the rules must “be sufficiently specific to ensure that determinations are equal and uniform.” TEX. TAX CODE § 11.31(g)(2). In the *Hurt v. Cooper* case cited by the ED, the Texas Supreme Court held that a tax must treat taxpayers within the same class alike, and that classifications may not be unreasonable, arbitrary, or capricious. *Hurt v. Cooper*, 110 S.W.2d 896, 901 (Tex. 1937). A two-part test is used to

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<sup>7</sup> The current version of § 17.17(2) requires that the applicant be informed of any deficiency “as soon as practicable.”

determine if taxation is equal and uniform: “(1) whether the tax’s classification is reasonable; and (2) whether, within the class, the legislation operates equally.” *R.R. Comm’n of Tex. v. Channel Indus. Gas*, 775 S.W.2d 503, 507 (Tex. App.--Austin 1989, writ denied). The ED’s negative use determination results in unequal and unfair operation of the Proposition 2 program within the class of HRSG owners. The Commission has granted 100% positive use determinations to the owners of 19 HRSGs that are substantively identical to and have the same air pollution reduction benefits as the HRSG identified in Ennis Power’s Proposition 2 application.

The ED explains that it issued the prior HRSG positive use determinations “in error” and that the disparate treatment of HRSG owners under Proposition 2 does not violate constitutional uniform taxation principles, because the ED is correcting that prior error. OPIC states that the ED’s position “evolved over time.” The cases cited by the ED, however, do not support the ED in the present matter.

The ED is correct that the Commission can change its interpretation and enforcement of a rule. However, in the *Grocer’s Supply* case cited by the ED, the Austin Court of Appeals made a pointed distinction between (A) the Comptroller’s substitution of one interpretation of a rule for another and (B) a change that contravenes one of the Comptroller’s existing rules. *Grocer’s Supply Co., Inc. v. Sharp*, 978 S.W.2d 638, 642 (Tex. App.--Austin 1998, pet. denied). The ED’s new position on HRSGs under Proposition 2 contravenes both Chapter 17 *and* the Texas Tax Code, which establishes that the question to be determined for HRSGs under Proposition 2 is whether they are “wholly or partly” used for air pollution control. *See* TEXAS TAX CODE § 11.31(k) & (m). The *Grocer’s Supply* court would not grant deference to or uphold the ED’s change in position. Moreover, the *Grocer’s Supply* court notes that statements made in the Texas Register at the time of rule adoption are not part of the rule itself and do not get the same deference as rule language. *Grocer’s Supply*, 978 S.W.2d at 642 n.6. Nothing said in the rule preamble would make the ED’s change-of-position regarding HRSGs equivalent to the “substitution of interpretation” that was approved by the *Grocer’s Supply* court, given that the change contravenes the treatment of HRSGs in the Tax Code.

The circumstances in *First American Title v. Strayhorn* can also be distinguished from the ED’s treatment of HRSGs under Proposition 2. *First Am. Title Ins. Co. v. Strayhorn*,

169 S.W.3d 298 (Tex. App.--Austin 2005), *aff'd on other grounds sub nom First Am. Title Ins. Co. v. Combs*, 258 S.W.3d 627 (Tex. 2008). The ED describes the Austin Court of Appeals as upholding the Comptroller's right to change her interpretation of a statutory tax scheme -- *as long as the new interpretation does not contradict the statute or a formally promulgated rule*. Here, as stated above and described more fully in Section III, the ED's new position on HRSGs *does* contradict the governing statute. The law does not grant the ED the right to shift positions on a tax issue like this one where the decision contravenes the Tax Code. *See Texas Citrus Exch. v. Sharp*, 955 S.W.2d 164, 170 (Tex. App.--Austin 1997, no pet.).

## **VI. Formal Rulemaking Is Necessary to Remove HRSGs from Proposition 2 Consideration**

The ED argues that a rulemaking was not necessary to issue the HRSG negative use determinations, and characterizes his action in making a sweeping decision regarding HRSGs under Proposition 2 as the result of case-by-case review of each pending application. The ED's argument ignores the fact that this change is not just a series of coincidentally timed individual denials, but rather an across-the-board policy change that has, without formal rulemaking, removed HRSGs from the Expedited Review List in Chapter 17.

HRSGs are listed in Texas Tax Code § 11.31(k) and, as a result, in the Expedited Review List in Chapter 17. *See* Figure: 30 TAC § 17.14(a), Part B (2008 version) & Figure: 30 TAC § 17.17(b) (current). Both the Texas Tax Code and Chapter 17 recognize the TCEQ's authority to remove an item from the Expedited Review List. *See* TEX. TAX CODE § 11.13(l); 30 TAC § 17.17(b) (current). However, such a removal must be accompanied by a Commission finding of "compelling evidence to support the conclusion that the item does not provide pollution control benefits." *Id.* No such finding has been made with regard to HRSGs, and the TCEQ has not removed HRSGs from the Expedited Review List or initiated the procedures to remove HRSGs from the Expedited Review List.

Removing HRSGs from the Expedited Review List in Chapter 17 requires formal rulemaking. The ED's across-the-board actions regarding HRSGs contravene the requirements of the Texas Tax Code, Chapter 17 *and* the Administrative Procedure Act ("APA"). Under Texas's APA, a rule is any "state agency statement of general applicability that . . . implements, interprets, or prescribes law or policy." TEX. GOV'T CODE § 2001.003(6). The TCEQ must promulgate new rules through formal rulemaking, including public notice and comment,

submitting to legislative review, and the Commission entering an order to adopt the rule change. TEX. GOV'T CODE §§ 2001.023; 2001.29; 2001.032-.033. Agencies must provide notice of a proposed rule with sufficient information so that interested persons can determine whether it is necessary for them to participate in order to protect their legal rights and privileges. *Tex. Workers' Comp. Comm'n v. Patient Advocates*, 136 S.W.3d 643, 650 (Tex. 2004).

The ED's decision effectively removed HRSGs from the Chapter 17 Expedited Review List, and that decision is invalid because it did not follow the procedures that the Texas Tax Code, Chapter 17 and the APA require for such a change. And because the ED's across-the-board decision regarding HRSGs contravenes the Tax Code and Chapter 17, the cases cited by the ED in his response brief do not support the ED's authority to make this change.

The agency action upheld by the Austin Court of Appeals in the *Texas Mutual* case cited by the ED can be distinguished from the ED's treatment of HRSGs, because the agency action in *Texas Mutual* did not contravene an existing agency rule. *Texas Mutual Ins. Co. v. Vista Community Medical Center, LLP*, 275 S.W.3d 538, 555 (Tex. App.--Austin 2008, pet. denied). In *Texas Mutual*, the court held that a staff report of the Division of Workers' Compensation was not subject to APA as a rule "because it did not change or amend Rule 134.401; it simply mandated internal consistency when applying the rule." *Texas Mutual*, 275 S.W.3d at 556. Unlike the action taken by the Division of Workers' Compensation in *Texas Mutual*, the ED's across-the-board policy shift on HRSGs *does* change an agency rule -- the general determination regarding HRSGs directly contradicts the Tax Code and Chapter 17's Expedited Review List, and effectively deletes HRSGs from that existing TCEQ rule.

The ED's reliance on *WBD Oil & Gas* is also misplaced. The ED cites *WBD Oil & Gas* for the proposition that agency policies or rules that are *not* rules of "general applicability" are not subject to the APA. The ED's statewide HRSG determination is clearly a decision with general applicability. In *WBD Oil & Gas*, the Texas Supreme Court held that Railroad Commission field rules are not rules of general applicability, but rather "are an adjudication of the individual interests principally affected." *Railroad Comm'n v. WBD Oil & Gas Co.*, 104 S.W.3d 69, 79 (Tex. 2003). The court made that determination based on a comparison of field rules detailing spacing and proration requirements *in a specific reservoir and its own peculiar geologic formations* to Railroad Commission statewide rules that govern the

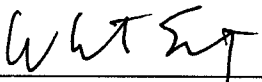
entire oil and gas industry. *Id.* The ED's decision regarding HRSGs, like Railroad Commission statewide rules, is a rule of general applicability. The ED's new HRSG position is not limited in geographic or any other scope. And while the ED states that his decision "affects a limited number of applicants for a use determination," his decision affects *every* current or potential future Proposition 2 HRSG applicant in the State of Texas. The ED's across-the-board rejection of HRSGs under Proposition 2 governs all Texas industry, and is distinct from the field rules that the Texas Supreme Court found to be exempt from APA requirements. The ED cannot make a statewide determination of general applicability that contravenes Chapter 17 on its face without complying with the procedures set forth in the Texas Tax Code, Chapter 17 and the APA.

## **VII. Conclusion and Prayer**

For these reasons, Ennis Power respectfully requests that the Commission overturn the ED's negative use determination for the HRSG installed at the Ennis Power Plant and remand the matter to the ED for a new, positive use determination that recognizes the significant air quality benefits and pollution reductions achieved by Ennis Power's HRSG.

Respectfully submitted,

BAKER BOTTS L.L.P.

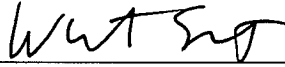
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## CERTIFICATE OF SERVICE

I hereby certify that I have served a true and correct copy of the foregoing *Ennis Power Company, LLC's Reply to the Response Briefs Filed by the Executive Director and Public Interest Counsel* on the following parties via U.S. Mail on this 30th day of October, 2012.



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